RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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Jan. 28, 1998 **LETTER 1244**

INFLATION/DEFLATION: *Newsweek* writes in its first January issue: "There are only two things that stand between the world and a vicious, deflationary bust: the International Monetary Fund acting as the *lender of last resort* and the United States of America acting as the *buyer of last resort.*"

That may be the story, but I'm not convinced. I note that gold appears to be bottoming while the bonds have backed off. Japan's Nikkei stock average has climbed above 16,000 again (the Jan. 9 low was 14,455), and Asia's stock markets may, just may, have discounted the worst. Money is sloshing freely around the US (courtesy of the Fed), and real estate and the NFL are flourishing. So you have to wonder, with all the talk of DEflation, could INflation still be the boogie-man in the nation's future?

Well, so much for the inflation/deflation debate which can't be solved now. Actually I'm much more interested in whether US stocks remain within the happy grip of a primary bull market -- or whether the bear is close to waking up after his multi-year period of hibernation.

THE PICTURE: Almost six months have elapsed since the Dow's August high, and the stock market, ornery creature that it is, refuses to reveal its secret. The secret? Is the bull market still alive or did August 6, 1997 (the day of the Dow's record high) represent the start of a "stealth" bear market?

When the Averages are fluctuating below their bull market highs but above secondary lows, they are in the territory that I have termed "no-man's land." In other words, the market is in that frustrating area where we have to wonder whether everything is still in Goldilocks-land -- or whether "something wicked this way comes."

On the plus bull side, the Averages have **not** rendered a bear signal. To do that the Dow would have to break below its October low of **7161.15** and the Transports would have to violate **3004.58.** So far, the Averages haven't even come close to those levels -- which is clearly a major plus for the bulls. Another very important plus (and it's surprising me) is that my **Primary Trend Index (PTI)** has been hitting new record highs (see page 2 chart). The market will not go down on a trend basis as long as the PTI continues to hit successive new highs.

From the bears' standpoint, the main arguments are as follows: the extraordinary series of **declining Dow peaks**, which were shown on page 1 of the last Letter. Now a **fifth peak** was established on January 20 when the Dow closed at 7873.12, then turned down. This gives us a series of declining Dow peaks as follows: August 6 -- 8259.31; October 7 -- 8178.31; December 5 -- 8149.13; January 5 -- 7978.99; January 20 -- 7873.12. Mmmm, suspicious.

Another bearish argument: as the ever-vigilant Ned Davis notes, the Dow has been recording fewer new highs each year for the last four years. For instance, the Dow recorded 71 new highs in 1995, 44 new highs in '96, 39 new highs in '97 and no new highs so far in '98. Ned notes, "Record new Dow highs were still numerous last year, but **diminishing**, and that wasn't a good sign in 1929 and 1965."

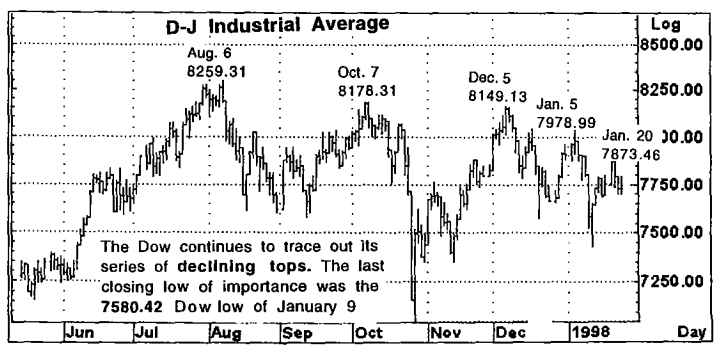
Jan. 16 DJIA 7753.55; PTI 5198; A-D Ratio +9.09
Jan. 23 DJIA 7700.74; PTI 5194; A-D Ratio +9.01
Dow Yield: 1.79%; Dow Price/Earnings: 20.1
Dow 144-day MA: 7716; Dow 34-day MA: 7798
Dow Times Book Value: 5.44; PTI 89-day MA: 5122
Percentage of Undervalued Blue-chips: 3%
Gold 34-day MA: 292

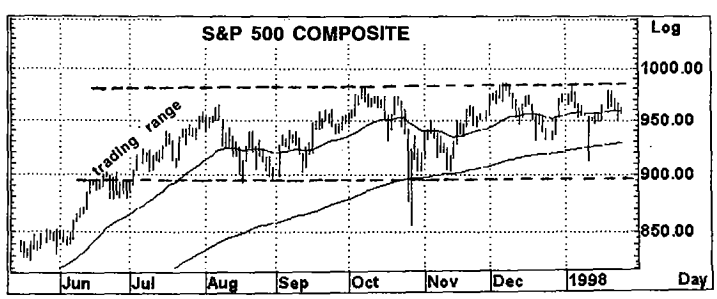
I've been paying particular attention to the action of the **advance-decline ratio** (see page 2 chart). The A-D ratio traces the trend of the **majority** of stocks on the NYSE. In my experience, there's nothing more important than a persistent trend in the A-D ratio. A rising trend in the A-D tells us that the majority of stocks on the NYSE are in up-trend. The reverse is true when the majority is in a declining trend.

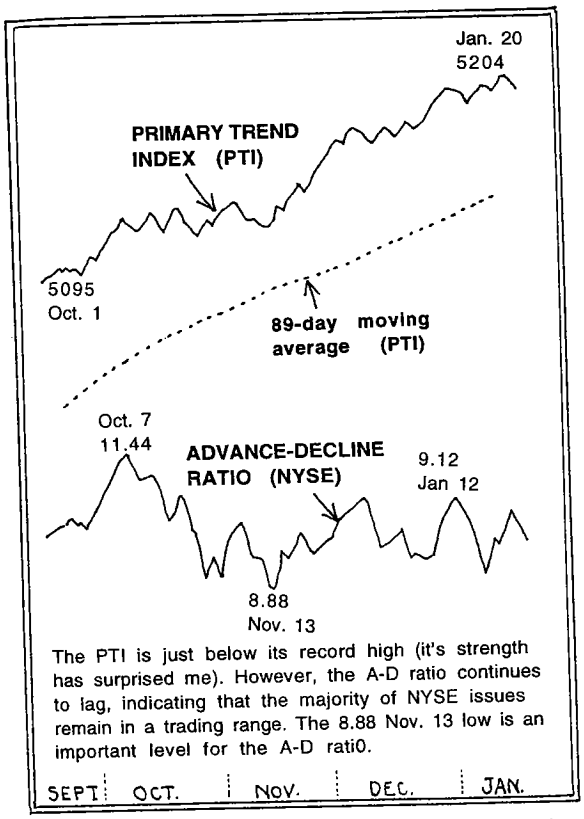
Interestingly, the A-D ratio recorded its high on October 7 at **11.44.** It then declined to a November 13 low of **8.88.** Since mid-November, the A-D ratio has been fluctuating between the October 7 high and the November low. Whichever way it breaks out will be extremely important for the trend of the entire market.

AN INTERESTING STUDY or WHY THE DOW RESISTS MAKING NEW HIGHS? Most investors tend to pay far too much attention to the news and activity of each trading day, rather than dealing with the big picture. One analyst who concentrates on the big picture is Peter Eliades of *Stockmarket Cycles* [(800)888-4351]. Peter does a lot of excellent original research, one item of which I want to discuss now.

First, a few fundamentals. A primary bull market will continue to advance until it has discounted the BEST that can be seen ahead. Once a bull market has discounted the best, there's no where to go but down. That "down" is what we term a bear market. Consequently, it's critically important to try to determine when, or at what point, a bull market has discounted the best that can be seen ahead.







The PTI is just below its record high (it's strength has surprised me). However, the A-D ratio continues to lag, indicating that the majority of NYSE issues remain in a trading range. The 8.88 Nov. 13 low is an important level for the A-D ratiO.

Many methods have been used -- most of them having to do with a violation or reversal of some well-established trend. For instance, the old standby was the Dow breaking below its 200-day moving average. Such a break usually implies a reversal of trend, but the trend-break could simply identify a correction, one that arrives early in a new bull market.

For identifying areas of **extremes of bullishness**, Eliades uses a method which I think is very logical. He keeps a count of the number of months the Dow has risen within a given time span. Eliades uses a time span of 100 months.

History shows than when the Dow has risen **68 out of 100** months, that's a very rare occurrence. Only **sustained, extreme bullishness** can bring that about. In fact, since 1900, only twice before has the Dow risen 68 out of 100 months. The first time was the period of October '61 through February '62. Result -- during the first six months of '62 the Dow dropped 26%.

Again in January, February and April of '66 the Dow was up 68 out of the preceding 100 months. The year 1966 marked the beginning of the great 1966-74 bear market.

Only once before did the Dow reach **69** up-months out of 100. That was in December '61. And as I said, that occurrence was followed by the violent decline during the first half of 1962.

Now here's the interesting part of the study. **In 1997** the readings (up-months out of the last 100) were as follows: January -- 68 (out of 100), February -- 68, March -- 68, April -- 68, May -- 68, **June -- 69, July -- 69,** August -- 68, September -- 68, October -- 68, November -- 68, December -- 68.

Do you remember the date of the **Dow high**? It was August 6, 1997, just a few weeks after the July reading of 69 up-months out of 100. But never in history have we seen anything like 1997, which produced a string of 10 months in a single year with counts of 68 up-months (two of 69) out of the last 100. On that basis, I must conclude that this is by far the most speculative, over-bought, overly-optimistic stock market in history.

The above study suggests to me that the Dow on August 6 at **8259.31** might well have discounted the best that could be seen ahead. True, the S&P, the NYSE Composite and the advance-decline ratio rallied to record highs two months later in October, but as this is written all are below their 1997 record highs.

RUSSELL OPINION: Until we receive either a Dow Theory re-confirmation of the bull market (i.e., new highs in BOTH Averages) or a Dow Theory bear signal (e.g., Dow below 7161.14, Transports below 3004.58), everything is opinion and guesswork, and don't let any expert or guru tell you differently.

What I think we may be in for is a long, frustrating series of rallies and declines, a period wherein stock group after stock group turns erratic or tops out -- but where the major averages hang on -- serving to keep the public hoping -- and buying.

Comments: One phenomenon that has me scratching my head is this: mutual fund money continues to pour into the market at the enormous rate of $25 to $30 billion every month. Mutual fund money is obviously public money and during most of the '90s this money has been instrumental in moving the market up. But since last June the stock market has been in a trading range, this despite the continued huge infusions of public money. Clearly, supply has been meeting demand, otherwise, the market would be at new highs. Question: who's been selling? Our only hint is that when dividend yields are thin, big (sophisticated) money tends to distribute, whereas when dividend yields are juicy, big money tends to accumulate.

This argument wouldn't have worked during most of the '90s when dividends were minuscule, but now there is a difference. The difference is that the market has been in trading range that has lasted for about six months -- six months without a new Dow high, three months without a new S&P high.

Conclusion: The one thing **different** about this market is the massive entrance and buying power of the public through mutual funds. Thus, even if a top is now in progress, **persistent buying** by the mutual fund public will serve to extend this top, extend it longer (in time) than any other top in history. Remember, however, that mutual fund buyers are now receiving **very low dividend returns.** Eventually, if their funds don't appreciate they will pull back on their buying. When that happens, the bull market will move towards a state of exhaustion. In other words, stock and fund buyers today are receiving very little return on their money -- therefore, in order for them to receive any kind of decent return, the market MUST go up.

A second observation: the **Dow** continues to be one of the **weakest** sectors of the stock market. Historically, it's not a good omen when the Dow (whose stocks tend to be held by knowledgeable, sophisticated investors) persistently **lags** the rest of the market.

I am showing two charts on page 1. The first is the Dow, and here we see the five declining peaks. Note that the Dow is now below its 34-day moving average (MA) which stands at 7807. The 144-day MA stands at 7716, and it would be a plus if the Dow could hold above the 144-day MA.

The second chart shows that broader S&P 500 (Mar. futures), and the plus here is that the 34-day MA is well above the longer 144-day MA. However, most people don't realize it, but the S&P has actually been in a **trading range** ever since last July.

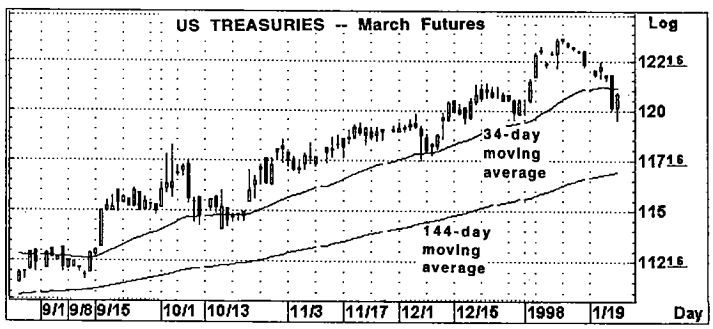
This is strictly a **Russell guess.** The stock market will remain in a trading range for possibly many more months. But the BEST was discounted during August-October of last year; therefore, the eventual breakout of the trading range will be to the downside.

BONDS: One of the biggest questions in the minds of investors is inflation or deflation, which is another way of asking -- higher or lower interest rates? If you knew the absolute answer to that one, you'd be in position to reap a fortune (via taking a position on bond futures). Unfortunately, I don't have an absolute answer, and I look to the bond market to provide me with an answer.

The bond market went into '98 in a bullish but extremely overbought state, with the 30-year T-bonds at record highs. The accompanying chart shows the bonds (Mar. futures) peeling off from their Jan. 12 high. This may be a result of **(1)** bonds being overbought or **(2)** a sharply lower dollar or **(3)** a reflection of the Clinton crisis. Remember, the dollar and T-bonds are extremely sensitive to perceptions of the health of the nation (and Clinton isn't helping any world view of this nation's health).

Merrill Lynch in its January 9 report states, "Why do we think the surprise for 1998 will be how far the yields will fall? The short answer is that we think that the worldwide liquidity trap that has been building for a decade is about to snap shut. Here are some key elements in that view: production is running well ahead of consumption, prices continue to weaken, and it is becoming increasingly costly for companies to hold inventories; investment spending isn't likely to stay at its recent torrid pace; and a worldwide surplus of funds will be searching for yields in the US, in the months ahead. In addition, mortgage growth is slowing, despite declining interest rates and booming consumer confidence, a sign that housing investments may be peaking for this cycle."

Russell Comment: The bond picture will probably rest on how much deflation Asia exports to the US. If deflation really does become a problem here, the Fed will move to lower rates. Greenspan has brought up the matter of potential deflation -- but I believe the Fed is still zero-ing on the inflation scenario (the Fed is well aware of the surging money supply plus the tight labor market -- and RISING GOLD).



INVESTMENT POSITION: I could easily keep the bull in the box, keep him here until or unless I receive an actual Dow Theory bear signal. The new highs in my PTI alone would justify that stance.

Nevertheless, with almost six months having elapsed without a new high in the Dow, I have to at least wonder about the underlying direction of the primary trend. Much as I hesitate doing it, I'm going to compromise by putting both the bull and a question mark in the box. In other words, the trend remains bullish, but there are enough legitimate questions about the bullish position to cause me to include the question mark as well.

My position is this: SIT TIGHT. If you have stocks, stay with them. There isn't enough evidence to indicate selling. If you have bonds, SIT TIGHT. They could be topping out, but I believe they're just correcting (the bonds having rallied too far above their moving averages). New money -- I feel stocks in general are overvalued and that the risk/reward on the upside is too limited. Personally, I'm putting all new money in T-bills, anything from 91-day to one year.

Comment: If the Dow itself is not able to make a new high, this market will not be able to mount a major move on the upside. The strongest Dow stocks (these are the stocks that would have to lead on the upside) are T, KO, DIS, GE, MRK, PG, JNJ, WMT.

NOTES & QUOTES: Clinton again -- and again. Questions: **(1)** Why was Ms. Lewinsky, an unpaid intern at the White House, given "top secret" clearance? **(2)** Why was Clinton's personal secretary the one who authorized Ms. Lewinsky's access to the White House? **(3)** Why was Ms. Lewinsky visiting the White House AFTER her job there was over (had she lost something)? **(4)** How can Hillary continue to put up with all this? **(5)** What possibly impelled Clinton to do what he did (assuming, of course, that he is guilty)? Answer to this one -- like all egotists, Clinton started to believe that he really was the "Teflon President." **(6)** What will Clinton do now? Possible answers to the last question: **(A)** Clinton could mount an all-out war on Saddam Hussein, thus deflecting adverse publicity. **(B)** Clinton could declare himself a "sex addict" (and seek treatment, thereby throwing himself on the legendary mercy and understanding of the American people). **(C)** Clinton could continue to do what he's done all along -- lying and denying. **Russell's last question** -- if Clinton is forced out of office, am I truly ready for Al Gore?

* *

A reader asks if I'm ready to alienate all my Democratic readers (and I have a lot of them). Answer: C'mon, do you want a milk-sop or a man with real opinions? Furthermore, I loved Harry Truman, and he was a Democrat, so there.

* *

Possibly the biggest "what if" in the world economic picture is whether China will devalue its currency again or perhaps just allow it to depreciate. China's economy (real GDP growth) has been slowing ever since 1992, but now China is dealing with massive unemployment. Even worse, with thousands of government-held businesses slated to be shut down, tens of millions of Chinese workers will face unemployment in the months and years ahead. Thus, the pressure to make the yuan more competitive by lowering its value will become almost irresistible. In the end, say experts, China will do what's best for China, and that means it will do everything it has to -- to increase employment, which means a lower yuan and increased exports. If the yuan does devalue, that could set off a whole new series of competitive devaluations across Asia. Note: two-thirds of China's exports in '97 were slated for nations now being hurt by the Asian currency crisis . . . China has a $240 billion inventory overhang, compared with $60 billion in the US.

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From a "World View" article in the *Washington Post:* "With the distractions of the holidays out of the way, it will become clearer that the Iraqi dictator has succeeded for more than three months in thwarting UN inspectors looking for chemical and biological weapons, while international concern has intensified about the harshness of economic sanctions on Iraq's civilians. Time is now working on Saddam Hussein's side, not Bill Clinton's. If Clinton accepts for much longer the New Year's status quo -- UN inspectors back in Iraq but ineffective, international support weakening for existing sanctions and opposition to US military action steadily growing abroad -- it will be Clinton in the box, not Saddam Hussein."

* *

I was hoping that we could get through 1998 without Clinton trying to socialize something else and extend the government's power. No such luck. Clinton plans to vastly expand the nearly broke Medicare system by lowering the age limit and setting a price ceiling for new participants. Presidential candidate Forbes responded, "Step-by-step, the Clinton-Gore Administration is trying to take over the American health-care system and socialize it so that it can be run by government bureaucrats, not physicians and patients." **Russell comment:** It's really unbelievable -- while half the world

agonizes over troubles caused by their incompetent governments, the Clinton Administration persists in trying to expand government's power over the American people.

Another item that's bothered me has to do with Clinton's labeling the '80s the "decade of greed" (of course, today the spread between rich and poor is greater than ever). But here's the way I think it works. If a Republican is in the White House and the nation is booming, it's called "a decade of greed." But if a Democrat is in the White House and the nation is booming, it's called "the new prosperity."

* *

The frantic lengths the networks will go to are unbelievable (really sad) to hang on to their shrinking audiences. The NFL contract with the broadcasters runs to a mind-blowing $18 billion over 8 years (wags said that for $18 billion the networks could buy the 30 NFL teams and their stadiums). But you can bet that team owners will still be pressuring NFL cities for taxpayer's money to build new stadiums ("build it or we'll move the team to, uh, somewhere else"). Expectations with all this new money coming in is that the NFL salary cap might rise 25% and players' salaries will then surge even higher. NBC (which is out of NFL broadcasting) predicted that the other networks would lose up to $200 million a year on the new contract. Ironically, the NFL take was so huge that it caused the Cincinnati Bengals' owner to say, "When you're in partnership with someone, it should be good for everyone. I worry about the networks. If it isn't good for them, then what happens down the road when the worm turns and we're the ones bargaining from weakness?" The value of an NFL expansion team is now expected to climb to $300 million, more than double the $140 million the owners of Jacksonville and Carolina teams paid to get into the league. This obviously affects Cleveland, which is expected to get an expansion team in '99. Comparisons: MLB received $1.7 billion from the broadcasters over five years; the NBA got $2.64 billion over four years; the NHL got $217 million over five years; and the NCAA basketball tournament got $1.74 billion over eight years. The summer Olympics got $456 million. It's clear that football is king of broadcasting TV.

Of course, the real problem is that broadcast TV's viewership is declining as Pay TV (e.g., HBO, Showtime, Cinemax) increases. NBC lost out on football and is also losing the hugely profitable "Seinfeld." Don't worry about Jerry Seinfeld (even though the poor guy can't seem to find a girlfriend). Under a proposed new contract for reruns, Seinfeld, who has a 20% stake (with a Time Warner unit) as a producer and creator, stands to make $50 million a year above the $1 million an episode he gets for starring in this year's series. **Russell comment:** Hey, maybe I should be writing for TV instead of writing about the markets?

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I read somewhere that kids who have parents who'd gone through the Depression or a war have an advantage in that their parents had the experience of surviving hard times. I guess I believe it. I grew up during the Great Depression of the '30s. During World War II I spent my youth in the Army Air Force as a combat bombardier (12th Air Force in Italy). I survived the war, later went through divorces (two of them), had five kids, one of them autistic, also survived a heart attack, quintuple by-pass, two motorcycle crashes (I quit riding this year) and a few other assorted disasters. Happily, I'm still here, still checking in. The old adage runs, "Whatever doesn't kill you makes you stronger." On that basis I should be a combination of Samson and Charles Atlas, but nah, I'm just a survivor with a healthy attitude.

I don't know if all that helped my kids. I still have to tell them to turn out the lights and wash the cars themselves instead of going to a car wash. I get annoyed when my kids order dollar cokes with their dinners at a restaurant, and I tell them that they're wasting money at theaters when they could be watching the same movie six months later on their VCR. They laugh at me and call me "a dinosaur" because I still act as if a dollar is worth something. Worse, my kids think I'm crazy because I prefer listening to Benny Goodman to Fiona Apple.

There's more. The other day I came out of the bathroom singing an old 1940s song, "When the Lights Come on Again All Over the World." My young wife, Faye, asked me, "Where'd you hear that one?" I answered, "Listen, embryo, that's an old pop tune written during the War. You weren't around when people sang that." And it's strange, even amazing, that the event that scarred so many of us is almost forgotten today (unless you watch the great war documentaries that appear weekly on the Discovery channel).

A great many of my readers are probably under 50 so you don't know too much about World War II. The scope of it, the horror of it, was beyond description. It involved almost everyone everywhere on the face of the globe. Example: the ferocious battle between Russia and Nazi Germany was the most gigantic military struggle in world history. It is estimated that 47 million people were killed in that battle alone and Russia counted 29 million dead. In contrast, all of Napoleon's battles were responsible for roughly one million killed.

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I've got about 9,000 subscribers now, and a lot of you, unfortunately, are going to face heart trouble (America's #1 killer). On top of that, a lot of you are be going to deal with doctors who recommend by-pass surgery or angioplasty, neither of which are permanent solutions to blocked arteries. So here's my recommendation. Order the *Alternative Medicine Guide to Heart Disease,* by Burton Goldberg [(800)333-HEAL]. Read the book, with particular attention to EDTA chelation. Then if you're still skeptical, go ahead and have a by-pass or an angioplasty or whatever your doctor suggests.

Oh yes, if you're even considering chelation, don't tell your doctor about it. Twenty-to-one he's had no personal experience with chelation, but he'll give you the approved medical answer and tell you it's never been proven. I get chelated every month, and 10 doctors (secretly) also take chelation treatments at the same place I do. It works.

U.S.' Heart Disease Bill Estimated At $274.2 Bil

Heart disease is expected to cost the nation $274.2 billion in 1998, up 6% from $259.1 billion in 1997, the American Heart Association reported. The total includes medical treatment, as well as lost productivity from people who die or become ill. The main reason is weight and diet. During a 1988-94 study, 65.7 million Americans exceeded the healthy weight range as defined by U.S. dietary guidelines.

People ask me why in the world the medical fraternity is against chelation. One reason is that if it works, it's going to cost physicians and hospitals a fortune. So why go to the expense of finding out if it works? But the truth always emerges and eventually the medical profession will have to deal with chelation, but until then they'll fight it with rumors, bad-mouthing, and unsubstantiated "facts." Here's a squib which tells us how much is involved in the "heart business." Believe me, the heart business is big-time.

* *

Stocks, bonds: Here's a little basic theory which all of my subscribers should understand. If you knew you would live a very long time, say 150 years, there'd be no sense buying anything but government bonds and then simply compounding and reinvesting the interest on those bonds. You'd end up a millionaire in due time, guaranteed simply through the "miracle" of compounding. And there would be almost no risk, unless the government itself defaulted on its debt.

What about stocks? Basically, stocks constitute, hopefully, a way to **"get there faster."** In other words, since stocks entail risk, the main reason to buy stocks is that stocks can build your fortune **faster** than bonds. Of course, this is only true during a bull market. In a bear market, stocks are going to melt your fortune away, but for today's investors that doesn't seem possible. Remember, since 1982 we've never had a year when the Dow

broke below the low of a preceding year. Or if you want to look at it another way, the Dow hit a low of 161.60 in 1949, and since then the stock market has gone persistently but irregularly higher.

Of course, there have been periodic "problems" such as the bear market of 1946-49, the crushing bear market of 1966-74 or even the declines during the early '80s. But if you were brilliant enough and had stomach enough to hold through thick and thin from 1949 to the present, you would have done wonderfully well, assuming you were smart enough to pick the right stocks.

But the point I want to make is that, consciously or unconsciously, what you're really doing when you buy stocks instead of bonds is -- you're **trying to beat time**, trying to beat the certainty (but the longer time needed) of making a fortune through compounding bonds and bond interest.

The disaster, the great tragedy, occurs if you lose your money in the stock market. When that happens not only are you losing your hard-earned capital but you are placing yourself far behind in the time cycle.

And at this time I guess I should remind newer subscribers of the win/loss paradox. Which is as follows -- if you have $10,000 and you lose half of it, that represents a 50% loss. But to bring that remaining $5,000 back to $10,000 again, you have to generate an increase of 100%. Not only do you have to double your money, you have to do it after taxes. So let me put it this way -- losing your capital in the current punitive tax system is a disaster, because you have to make so darn much to just get back to even again. Or as your accountant might put it, "You win and the government is your partner; you lose and buddy, you're on your own."

A few facts: From its peak in 1966, the Dow fell 38%. It took 7 years until 1973 to get back to even. Then, from the peak in 1973 the Dow then fell 45%. It took the next 10 years until 1983 to get back to even again.

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The balanced budget talk is rampant again. Of course, the politicians don't talk about how the budget is balanced, which is courtesy of robbing the Social Security trust. No, the pols are too excited about spending "the coming surplus." Actually, here's the story. The national debt last week was $5.486 trillion. One year ago it was $5.312. That means that in the last 12 months the government added $174 billion to the national debt. The **interest** alone on the national debt is now $250 billion a year.

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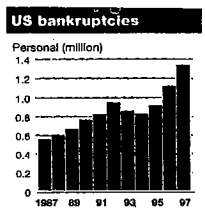
Help! The roads and freeways are so packed with sport-utility vehicles and trucks that in my little SLK I can hardly see where the devil I'm going. Now BMW, forced to compete with Mercedes' new super-popular sport-utility vehicle, announces that it too is going to build a SUV. Great, SUVs and larger, the ultimate yuppie vehicles, they're a pain in the can as far as I'm concerned.

* *

What the biggest financial trend in the US today? Easy, it's filing for bankruptcy. Last year citizen bankruptcies shot up 19% year-over-year to 1.34 million individual bankruptcies, the highest in the nation's history, even including the Great Depression. There's even a toll-free phone number for bankruptcy info, it's 1-800-BANKRUPT. They used to say, "Bottoms up," now they say, "Belly up."

US citizens go for broke over nation's latest trend

By Richard Tomkins in New York



Forget cigar lounges, Beanie Babies and sports utility vehicles. The hottest trend sweeping the US is filing for personal bankruptcy.

According to figures published by the Visa payment card association yesterday, the number of Americans declaring themselves bankrupt shot up by 19 per cent to 1.34m last fewer than 30,000 people declared themselves bankrupt in 1995, representing about one in 2,000 of the population.

One reason is that bankruptcy is a relatively painless exercise in the US, and has come to be regarded as a sensible financial planning tool rather than a cause for shame or disgrace.

Across the US, lawyers place advertisements inviting people to solve their financial prob-

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Revisions: It turns out that Japanese banks have about three times the amount of bad debts than were originally announced. The latest figure is that Japan's banks are holding an astounding $625 billion worth of non-performing loans. With it all, the Japanese stock market is showing signs of having discounted the worst.

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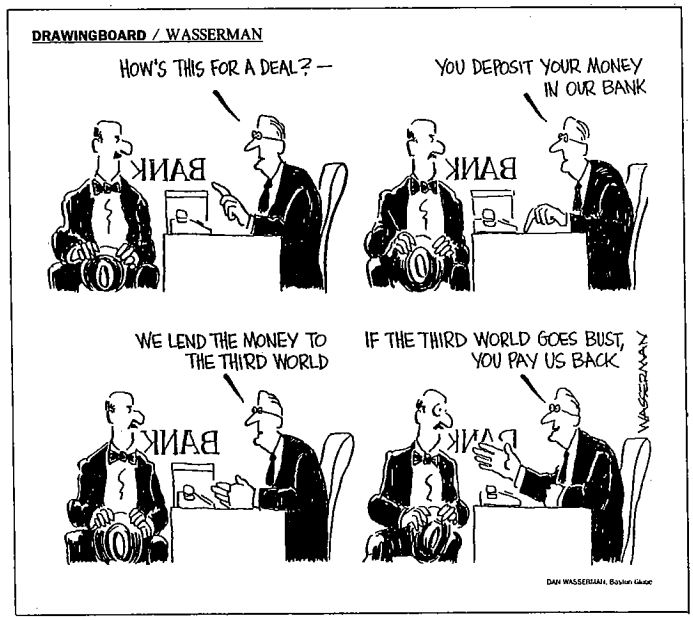
IMF bailouts: We give the money to the IMF, and the IMF lends it with strictures to various busted nations. What are the IMF demands when it lends money? The nation must take steps to reduce its debt, they must increase taxes, reduce government spending, devalue their currencies and reduce their imports. But many economists claim this harsh "medicine" simply makes matters worse. Now both liberal Democrats and conservative Republicans are stepping up criticism of the bailouts. Many object to using taxpayers money to bail out foreign nations. And the more libertarian-minded object to the interference of the US and the IMF and they want to let the free market system works its way. States GOP Senator Lauch Faircloth of N. Carolina, "The free market is no longer at work in the field of international finance. We have privatized the gains and socialized the losses."



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If you're a foreigner and you have the dough, can you buy yourself into a **US citizenship**? Yes, green cards are for sale. These coveted cards confer legal status as a US resident and constitute the first step towards citizenship. It's part of a US program to encourage immigration by wealthy foreign investors. The investor visa program, passed by Congress in 1990, reserves up to 10,000 green cards a year for investors and their immediate families. To qualify, the principals must each establish at least 10 full-time US jobs by investing $1 million -- or $500,000 if the jobs are in certain high-unemployment areas -- in the start of a business or the rescue or expansion of an existing one.

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How many people inhabited the earth at the times of Christ? The estimate -- 250 million, one fourth of which lived in China. The world's biggest city in 1000 AD was Cordova, Spain, with 450,000 residents. The world's population after 1000 AD grew by a sluggish one tenth of 1% until 1700, when modern medicine first appeared. Even in 1700, half of all children died before the age of 5. By 1798, there were 800 million people in the world. That year Malthus, a British economist, wrote that famine, disease and wars would keep the population at minimum, supportable levels. Wrong, the earth now supports almost six billion people. But growth rates are now subsiding due to a global trend towards smaller families. The twentieth century has been the bloodiest century in history with hundreds of millions of people having died due to wars, genocide, and disease.

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The two largest mutual funds have halted their **daily** reports on cash flows into their funds. Fidelity and Vanguard have stopped this procedure because industry watchers monitored flows into specialist funds and used the information to recommend sectors and sometimes individual stocks. As a note of interest, Fidelity now has about $600 billion under management.

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It's been shown that being a vegetarian will lower both your weight and your cholesterol. And the search goes on for meat with a lower fat content. A 100 gram serving of beef (about 3.5 ounces) contains around 10 grams of fat. The same size of buffalo meat has 2.4 grams of fat. Ostrich has only 2 grams of fat while kangaroo has only 0.5 grams of fat. Exotic or alternative meats are gaining a bit but are nothing compared with beef. In all of '97, 20,000 buffalo were slaughtered (the US buffalo population is approximately 250,000). But get this, cattle here are slaughtered at the incredible rate of 130,000 **a day.**

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How do government agencies justify their existence? By issuing more regulations. How's this for one of the most insane federal regulations ever? The National Highway Traffic Safety Administration announced last week that it will start requiring **golf carts** to have seatbelts, windshields, turn signals and rearview mirrors.

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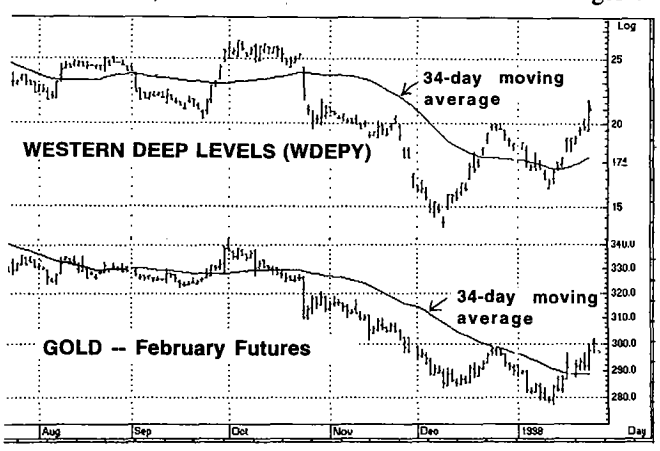
GOLD: First, there are two kinds of deflation. **(1)** The price level of goods declines due to **vicious competition.** This is the type of deflation or dis-inflation we're experiencing now. **(2)** Due to a **scarcity of money**, the economy is squeezed (as per the early-30s) and the price of everything sinks lower. There's no lack of money in the US today, what there is a lack of pricing power.

So Question: Is it possible that all the current deflation talk is fated to be wrong? After all, the US M-3 broad money supply is still surging at an almost 10% rate (on a year-over-year basis). The Asian situation may be scraping bottom. Auction prices in the US are healthy, real estate prices are moving up, apartment and condo prices are rising, luxury item prices border, in many cases, on the outrageous, and the cover of the Jan. 19 *New Yorker* magazine pictures a matron in a luxurious fur coat having fun -- she's riding down a snowy hill on a sled, a sled being steered by a uniformed chauffeur.

Back to gold. The value of gold as real money was never demonstrated more dramatically than in Asia over recent months (although gold detractors will never talk about this). The fact is that those who held gold in Thailand or Indonesia or Malaysia saw the price of gold explode in terms of their collapsing local currency. Their only problem was -- nobody was holding **enough** gold.

Talk is talk, but **prices** tell the story. The chart shows that gold (Feb. futures) has formed what looks like a real base. The preceding high close for the Feb. contract (Dec. 24) was 298. Therefore, any close above 298 would be impressive. Gold, as this is written, is rallying **above** its 34-day moving average. Some of the gold "oomph" is probably a reflection of Clinton's precarious position. After all, if the "leader of the free world" is in danger of being toppled, and the reserve currency of the "world leader" is the dollar -- well, some of this mess is bound to rub off on the dollar.

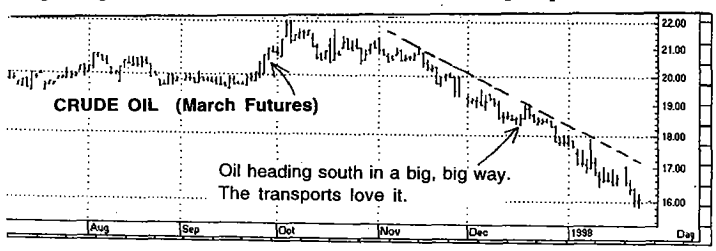


South African gold mines have had a very hard time of it, but the best of the S. African mines are looking a lot better. Western Deep Levels (NYSE) struck a extreme low of 14 on Dec. 9 (it was 56 at the January '96 high). Last week WDEPY not only bettered its last peak but it rallied to over 21. Thus Western Deep is up over 50% in less than two months. It reminds me of what my old friend, John Magee used to say -- **"Don't tell me what to buy, tell me WHEN to buy it."** What else do you know that went up 50% over the last two months? Second lesson: there's nothing like buying something that's totally hated (like gold and particularly a South African gold mine) at a time when its sold out and scraping the bottom and when all the experts are deriding it.

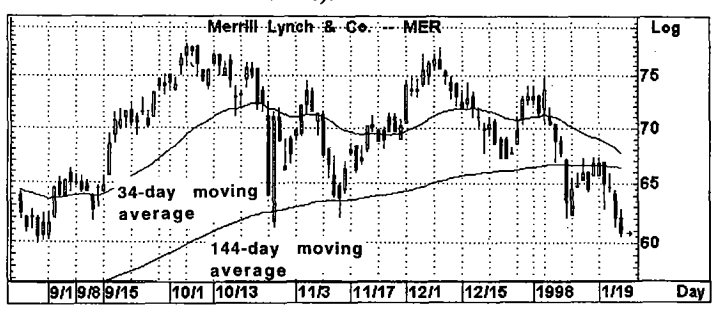
For those who want to jump the gun and take a limited position in gold, I continue to like Barrick Resources (ABX) and the two Canadian gold royalty stocks (Toronto exchange but quoted daily in the *WSJ*), Euro Nevada and Franco Nevada.

LATE NOTES: I think Ms. Lewinsky HAS to accept immunity from Mr. Starr. After all, if she had been telling the truth in her affidavit ("nothing happened") why would she need immunity at all? Her best bet -- save herself, take immunity and tell the **whole** truth. . . Faye and I were at the great XXXII Super Bowl, and I was amazed to hear the crowd hiss and boo when Clinton's pic was flashed on the screen. That, I believe, is the sentiment today.

A major reason for the strength in the Transports is the collapsing price of oil. Here's a chart of the March crude oil contract. I hear regular gas in Texas is as low as 95 cents at the pumps.



One stock that I have called a bellwether is giant Merrill Lynch. The brokers tend to be very sensitive to coming volume on Wall Street, which certainly provides us with food for thought when we study the bearish pattern in MER. On January 22 MER registered its lowest closing since last August. The stock appears to have been under distribution ever since its October high of 78 (MER is down 20% over the last four months).



The D-J Transports hit a record high of 3368.33 on October 21. Then two weeks ago, on January 20, it looked as though the Transports would close at a new record high, but as the session wore on, the Transports backed off, closing at 3366.52 -- less then 2 points under their January 20 record peak. At this high level, a 2-point difference is almost statistically insignificant. Frankly, I don't know whether or not to take the January 20 close as another high by Transports, a high again unconfirmed by Industrials. Suffice it to say that the Dow is not confirming the Transports' strength, and this is a caution signal. As this is written, the Dow is more than 500 points below its bull market high of 8259.31, recorded almost six months ago on August 6. Not good.

NEXT MAILING: Feb. 11, 1998